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COURT OF APPEAL, FOURTH APPELLATE DISTRICT

DIVISION ONE

STATE OF CALIFORNIA

DIABETES RESEARCH RESTITUTION,
LLC,

Plaintiff and Appellant,

v.

WILLIAM WACHTEL et al.,

Defendants and Respondents.

D069796

(Super. Ct. No. 37-2012-00090260-
CU-BT-CTL)

APPEAL from a judgment of the Superior Court of San Diego County, Ronald L. Styn, Judge. Affirmed.

Shustak, Reynolds & Partners, Paul A. Reynolds; Edleson & Rezzo and L.B. Chip Edleson for Plaintiff and Appellant.

Wachtel Missry and Elliott Silverman for Defendants and Respondents William Wachtel, EuroAmerican Investment Corporation, Peter Knobel and Knobel Children's Trust.

Keker & Van Nest, Susan J. Harriman, Matan Shacham and W. Hamilton Jordan for Defendant and Respondent John Hagenbuch.

After acquiring the litigation claims of a former biotech company called MicroIslet, Inc. (MicroIslet), Diabetes Research Restitution, LLC (DRR) sued several individuals who were formerly associated with MicroIslet. In its operative complaint, DRR alleged a claim for breach of fiduciary duty against a group of former MicroIslet directors and officers and a claim for aiding and abetting breach of fiduciary duty against several of the company's former creditors. Both claims were based on allegations that the officers and directors pursued a wrongful takeover scheme, eschewing available equity financing in favor of onerous debt financing that would result in a recapitalization plan giving the debt holders control of MicroIslet.

The instant appeal only concerns the claims against certain creditor defendants: John Hagenbuch, William Wachtel, EuroAmerican Investment Corporation (EuroAmerican), Peter Knobel, and the 1996 Knobel Children's Trust (the Trust) (Hagenbuch, Wachtel, EuroAmerican, Knobel, and the Trust collectively Respondents). Respondents successfully moved for summary judgment as to the aiding and abetting claim.

DRR appeals the final judgment in favor of the Respondents only. DRR contends a triable issue of material fact exists as to its cause of action for aiding and abetting breach of fiduciary duty for each of the Respondents. We disagree. DRR has not shown that a triable issue of fact exists as to any of the Respondents' actual knowledge of the specific breach of fiduciary duty alleged. Thus, we affirm the judgment.

FACTUAL AND PROCEDURAL BACKGROUND

John Steel IV founded MicroIslet in 1998. MicroIslet was a Nevada corporation with its headquarters in San Diego. Steel was the company's original chairman of the board and chief executive officer (CEO). MicroIslet was a biotechnology company with the goal to develop and sell a treatment for juvenile diabetes, based on a patented islet transportation technology licensed from Duke University. MicroIslet's proposed treatment involved transplanting pancreas cells from pigs into human beings. The development of this treatment was arduous, the regulatory hurdles were high, and the technology daunting. For example, the Food and Drug Administration (FDA) placed rigorous demands on all companies seeking to develop new medical treatments, and this was especially true of MicroIslet's desired treatment, which would involve treating humans with live cells from another species.

Because it was attempting to develop a new treatment, MicroIslet required and spent large sums of money. As such, funding the company was a constant concern. Although MicroIslet received some research grant revenue, it had to find other sources of funding. This need was even more critical because MicroIslet never produced any product revenue (the FDA never approved any MicroIslet product)¹ and MicroIslet lost money during every quarter of its existence.

In 2002, Steel asked Hagenbuch, his brother-in-law, to invest in MicroIslet. Hagenbuch was a successful businessman and financial advisor who had served as board

¹ MicroIslet never reached the point of filing an investigational new drug application (IND) with the FDA.

chair and director of multiple public and private companies and nonprofit organizations. Between 2002 and 2006, Hagenbuch invested \$2.5 million in the company by purchasing almost four million shares of MicroIslet common stock. Hagenbuch became MicroIslet's second largest shareholder, after Steel, who received his shares as the company's founder and not based on any financial investment.

In 2003, Hagenbuch loaned money to MicroIslet because the company was again running out of money. In all, he loaned about \$500,000, the terms of which Steel, the company's CEO and chairman at the time, approved. The loans had a four-month maturity period. MicroIslet did not repay the loans, and Hagenbuch did not force repayment. Instead, Hagenbuch voluntarily converted the loans into common stock in November 2003.

From January 2006 to June 2007, Hagenbuch served as the nonexecutive chairman of MicroIslet's board of directors. While chairman, Hagenbuch did not receive compensation. During his tenure, Hagenbuch continued to attempt to raise funds for MicroIslet, but fundraising proved to be difficult. MicroIslet had not received FDA approval for its technology and produced no revenue.

In January 2007, Hagenbuch again loaned money to MicroIslet to allow the company to continue operating while it tried to secure equity financing. The loan was for \$2 million, subordinated and unsecured, priced at the Wall Street Journal prime rate, with a one-year maturity period, no penalty interest rate, and a grant of stock warrants. Hagenbuch told the company that, when it next obtained equity financing, he would convert his loan into equity on the same terms as the equity financing.

In March 2007, MicroIslet's outside counsel, Sheppard Mullin Richter & Hampton (Sheppard Mullin), informed members of the board that MicroIslet was operating in the zone of insolvency. Specifically, Sheppard Mullin indicated that the company had only "seven to nine weeks of cash remaining to sustain operations" and was spending about \$750,000 per month. In May 2007, Hagenbuch made a final loan to MicroIslet based on his understanding that the company would need those funds either to reorganize or wind up its affairs. The loan was for \$1 million, unsecured, priced at the Wall Street Journal prime rate, with an about eight-month maturity period and no penalty interest rate, and with a grant of warrants.

In June 2007, Steel and one of his friends Philip McConkey² proposed a plan to bring new leadership into MicroIslet. This new team was led by Ronald Katz and provided over \$1 million in financing (\$600,000 of this initial investment was provided by Katz). Katz was a prominent New York accountant, who had been a MicroIslet shareholder since 2003, previously investing about \$1.5 million in the company. Katz replaced Hagenbuch as the company's chairman of the board in June 2007. The other new board members included Keith Hoffman, Michael Andrews, and Brian Conn. Andrews became the CEO, and Conn was named the chief financial officer (CFO).

The infusion of over \$1 million from Katz and the other investors was not the panacea for MicroIslet's financial ills as it still owed \$1.5 million to its vendors and had

² McConkey was named as a defendant in the instant action. He is not a party in this appeal.

other debt on its books, including Hagenbuch's loans.³ The company therefore continued to need additional funding to keep operating.

MicroIslet's filings with the United States Securities and Exchange Commission (SEC) illuminated the company's history of significant losses and expected future losses. Based on the lack of funds, MicroIslet's SEC filing indicated that there was "substantial doubt about [its] ability to continue as a going concern." The SEC filings also warned investors that, even if MicroIslet obtained additional capital investments sufficient to remain operating, those investments could dilute the holdings of the existing shareholders. MicroIslet's officers continued to try to raise new capital with little success.

In 2008, MicroIslet fired its long time outside counsel, Shepard Mullin, and replaced it with the firm of Foley & Lardner. Sheppard Mullin had continued to advise the company that it was insolvent and should file bankruptcy. Katz and the other board members rejected Shepard Mullin's advice and hoped the company would be able to raise additional funds to allow it to file an IND.

In June 2008, MicroIslet hired the investment banking firm Scura Rise & Partners, LLC to try to raise \$15 million in capital through the sale of preferred stock. Although Scura Rise distributed about 100 private placement memoranda to potential investors and met with numerous potential investors, its efforts ultimately proved unsuccessful.

³ When Hagenbuch was replaced as chairman, he offered to convert his \$2 million loan into equity on the same terms the company had just raised. MicroIslet's management declined the offer.

After Katz become chairman, MicroIslet's officers and directors decided to have MicroIslet take on short term loans to keep the company open until it could file an IND.⁴ Katz himself loaned MicroIslet more than \$1.2 million and, as trustee of a trust known as the SMR Trust III (SMR), caused that trust to loan an additional \$2.5 million. Katz also solicited loans from his friends and business associates, including Knobel, Wachtel, and Harold Levine.⁵

Katz was acquainted with Knobel, a real estate developer who worked with Stephen Ross, a successful real estate developer in New York and the owner of the Miami Dolphins. Ross and Knobel were both clients of Katz's accounting firm, and Katz was one of the trustees of SMR, a trust for the benefit of Ross's children.

Katz first introduced Knobel to MicroIslet in 2003, and Knobel invested, both individually and on behalf of the Trust, hundreds of thousands of dollars in MicroIslet stock over the next few years.

Knobel did no due diligence into MicroIslet but, relying on the fact that Katz was a prominent accountant and that Ross, whom Knobel knew to be "a very shrewd investor" and a billionaire, had also invested in MicroIslet, Knobel decided to buy MicroIslet stock without further investigation.

⁴ After a positive meeting with the FDA, MicroIslet issued a press release announcing plans to file an IND sometime in the late third quarter of 2008. MicroIslet never filed any such application.

⁵ Levine currently is a defendant in the instant matter. He is not a party to this appeal. Thus, we do not discuss Levine's loans to MicroIslet.

After Katz became MicroIslet's chairman, he asked Knobel to loan money to MicroIslet, explaining that MicroIslet needed short term "bridge financing" to keep the company operating while it was seeking new equity investors. In September of 2007, Knobel loaned MicroIslet \$1 million. In June of 2008, in response to another request by Katz, Knobel agreed to loan an additional \$500,000, this time out of the Trust. Both loans (the one made by Knobel personally and the one by the Trust) bore 10 percent interest, with the interest rate rising to 24 percent if the loans went into default. In Knobel's experience, this was not an unusual interest rate for a speculative company such as MicroIslet. Knobel had both borrowed and lent money in his own businesses at similar rates. Ultimately, MicroIslet never repaid Knobel or the Trust any of the \$1.5 million they had lent it or any of the accrued interest.

Katz also was acquainted with Wachtel, a lawyer in New York. Wachtel's law firm represented Ross. Through his representation of Ross, Wachtel met Ross's accountant, Katz. Katz later became a client of Wachtel's law firm. Wachtel has been an attorney in New York since 1979. Beginning in 1984, he also has owned EuroAmerican, a merchant banking company, which makes loans to companies that cannot obtain conventional bank financing.

Katz asked Wachtel to loan money to MicroIslet. Wachtel agreed to loan money directly to Katz through EuroAmerican. Wachtel did so because he knew Katz personally, believed him to be a highly successful accountant, and thought Katz would repay him. Wachtel caused EuroAmerican to loan Katz over \$400,000 at an eight percent

interest rate. Unbeknownst to Wachtel, Katz reloaned this money to MicroIslet at a higher interest rate.

In August of 2008, Katz again asked Wachtel to loan money to MicroIslet. Katz told Wachtel that MicroIslet needed short term loans to keep operating until it could raise equity capital from investors. EuroAmerican loaned MicroIslet about \$1 million in 2008, at interest rates of up to 24 percent. Unlike EuroAmerican's loans to Katz, which Katz repaid, MicroIslet never repaid any part of its loans from EuroAmerican.⁶

While MicroIslet was seeking bridge financing, Hagenbuch's two loans remained debts owed by the company. In November 2007, about a month and a half before MicroIslet defaulted on his loans, Hagenbuch offered to extend his January 2007 loan for another year at the Wall Street Journal prime rate if the company paid him the interest he was due at that time and the principal of his May 2007 loan, but the board of directors did not accept his offer. MicroIslet defaulted on Hagenbuch's January and May 2007 loans in January 2008. Hagenbuch did not demand repayment of either loan at that time.

In mid-2008, Hagenbuch learned that MicroIslet had given a more recent creditor a penalty interest rate of 24 percent when the company defaulted on that creditor's loan. Hagenbuch approached Andrews about the discrepancy between the other creditor's penalty interest and Hagenbuch's loans. Ultimately, MicroIslet's board agreed to amend the terms of the notes for Hagenbuch's January and May 2007 loans. The amendment increased the penalty interest rate on the loans and extended the maturity dates. Even

⁶ Katz repaid the money EuroAmerican loaned him after Wachtel sued Katz.

though MicroIslet defaulted on his two loans, Hagenbuch did not demand repayment. MicroIslet never repaid any portion of Hagenbuch's January or May 2007 loans, including failing to make any interest payments.

Seeking bridge financing did not end MicroIslet's quest to find new sources of funding. The company's board also considered other alternatives. For example, on August 20, 2008, the board convened a meeting and resolved to form a special committee to "explore recapitalization alternatives in light of the Company's current capital structure and funding needs and to present to the full Board a plan of restructuring that would enable the Company to raise the additional funds necessary to execute on its current business plan." The special committee consisted of Andrews, Hoffman, Conn, and Adam Lenain (an attorney from Foley & Lardner). The next day, the special committee met to discuss alternatives and Lenain prepared a memorandum (Lenain Memo) summarizing the special committee's "initial recommendation."

The Lenain Memo noted that MicroIslet needed between \$4 million and \$5 million in new money to continue its operations until it could file an IND and get the FDA's approval, and would then need an additional \$10 million to \$12 million to complete the first phase of clinical trials. It further noted that the company's existing debt was deterring new investors from investing additional capital, and that a bankruptcy reorganization would wipe out the investments of all the existing shareholders. The special committee therefore proposed that existing creditors should agree to forbear on enforcing their notes, and instead convert those notes into a new class of preferred stock, and that MicroIslet should then issue \$4 million to \$5 million in new senior secured debt.

The purpose of the restructuring proposal was to make it easier for MicroIslet to raise new capital.

MicroIslet's board approved the proposal outlined in the Lenain Memo. It did so even though it was aware the proposed recapitalization plan would result in a substantial dilution of the existing shareholders with the company's creditors becoming major equity owners. Apparently, the board believed this approach was prudent because MicroIslet's debts surpassed its worth. As such, the company was "effectively already owned by the debt holder[s]." In addition, outside counsel had advised the board that, because the company was insolvent, the board owed a fiduciary duty to the creditors, not to the shareholders. Moreover, the board recognized that in a bankruptcy, the existing equity would be wiped out completely; so it was preferable for the existing shareholders to own 10 percent of a reorganized company rather than zero percent of a bankrupt company.

The Lenain Memo suggested a mechanism under Nevada law to adopt the restructuring proposal without a vote of the shareholders. Lenain explained that the company simply did not have the time or money to prepare proxy materials for a shareholder vote by a public company; before any shareholder vote could take place, "[t]he company would have been out of business." MicroIslet's board agreed with this assessment.

Katz sent a copy of the Lenain Memo to Wachtel. Wachtel did not provide Katz any advice regarding the memorandum's proposal.

MicroIslet's board formulated a proposed "Debt Harmonization Agreement" to carry out the proposed recapitalization of the company, and decided to propose it to the

company's creditors. A "presentation to debt holders" was prepared, but neither Wachtel nor Knobel attended it or received a copy of the written materials prepared for the presentation.

MicroIslet's board subsequently drafted a document entitled "Confidential Summary of Recapitalization Terms" (Term Sheet), summarizing the terms of the proposed recapitalization. The Term Sheet stated it was nonbinding, was "prepared for the purpose of seeking indications of interest only," and that no party would be bound until and unless "definitive documents are signed by all parties" and approved by MicroIslet's board.

Katz sent a copy of the Term Sheet to Wachtel and asked him to sign it. Knobel also received a copy of Term Sheet after he and the Trust had made all their loans to MicroIslet.

No final binding agreement embodying the concepts of the Term Sheet was ever drafted or executed. The conversion of debt to equity contemplated by the Term Sheet never occurred. Hagenbuch, Wachtel, and Knobel never converted any of their debt into MicroIslet stock.

In late 2008, MicroIslet could not meet its payroll or even pay the payroll service that prepared its employees' checks. At the same time, one of MicroIslet's clinical trials failed, delaying its ability to file an IND with the FDA. Further work on the IND was halted because MicroIslet could not pay the consultants who were preparing it.

On November 11, 2008, MicroIslet filed a bankruptcy petition seeking reorganization (11 U.S.C. § 1101 et seq.). Wachtel, through EuroAmerican, agreed to

provide "debtor in possession" financing to MicroIslet to allow it to continue to function while in bankruptcy. Despite MicroIslet originally filing for bankruptcy with the hope of reorganizing as a new, viable company, ultimately the company converted the bankruptcy petition to one seeking liquidation (11 U.S.C. § 701 et seq.). Although the details do not matter in the instant dispute, suffice it to say, disagreements between various interests impeded the success of MicroIslet's reorganization during bankruptcy.⁷

During the bankruptcy proceedings, Steel and others formed DRR, which purchased from MicroIslet's bankruptcy estate any litigation claims the company would have had before filing for bankruptcy. DRR then sued MicroIslet's former officers and directors as well as its creditors (including Wachtel, EuroAmerican, Knobel and the Trust) in federal court alleging, among other causes of action, violations of the federal Racketeer Influenced and Corrupt Organizations Act (RICO), 18 United States Code section 1962. The federal court dismissed the RICO claim with prejudice and DRR's state law claims without prejudice.

After the federal court's dismissal of its action, DRR filed a complaint in San Diego Superior Court. After Respondents' successfully demurred to the complaint, DRR filed a first amended complaint (FAC). In the FAC, DRR alleged that MicroIslet's directors and officers breached their fiduciary duty to the company. Specifically, DRR averred:

⁷ For example, the bankruptcy estate sued Steel for allegedly using MicroIslet's corporate credit card for a year and a half after his employment ended to charge personal expenses to the company.

"These Defendants breached each of these [fiduciary] duties. When it became apparent that MicroIslet was on the verge of becoming immensely valuable, the Defendants developed and pursued a scheme to steal the business by saddling it with expensive debt that could not and would not be repaid and that they could then convert to ownership. Rather than seeking or accepting available funding for the Company at competitive market rates or on favorable terms from existing shareholders and others, the Defendants arranged to make loans themselves or through friends and related parties and to provide financing to the Company on terms unfavorable and unfair to the business, all designed to cause the debt to go unpaid so that the Defendants would take over most or all of the ownership of the business from existing shareholders."

DRR further alleged in the FAC that, historically, MicroIslet had been funded by equity contributions rather than borrowing money. Per DRR, this approach changed when a Katz led investor group provided over \$1 million to the company and he became chairman and named six directors. DRR then claimed that the officers and directors took MicroIslet from a debt free position to one "saddled with significant debt of nearly \$7 million." DRR explained that these loans "were part of a plan . . . to dilute the debt they created into new equity ownership of the Company." In addition, DRR alleged that the officers and directors were "turning down offers of favorable financing" during the time in question.

In its second cause of action, DRR alleged that Hagenbuch, Wachtel, EuroAmerican, Knobel, the Trust, and other creditors not part of this appeal, aided and abetted the officers and directors in their breach of fiduciary duty. DRR averred:

"Katz informed several of his close friends and business associates about his scheme to steal the business. Specifically, after Katz concluded through his own investigation and sources that MicroIslet was on the verge of becoming immensely valuable, he shared his conclusions with several close friends and business associates and he

further shared his plan to steal the business away from its existing public shareholders by saddling the Company with expensive debt that could not be repaid. Katz explained to his select friends and business associates that they could profit from his scheme by also becoming creditors of MicroIslet, or by loaning him money to reinvest in the Company so as to become indirect creditors."

After the court overruled Respondents' demurrer to the FAC, Respondents answered the complaint. Later, Respondents moved for summary judgment of the aiding and abetting claim.

After considering the pleadings and evidence as well as entertaining oral argument, the superior court granted summary judgment in favor of Respondents. In doing so, the court determined that Respondents established the absence of a triable issue of material fact as to whether they had actual knowledge of the alleged "scheme to steal the business." In addition, the court found that Respondents also had shown the lack of any triable issue of fact as to the "conscious decision" element of an aiding and abetting cause of action.

The court subsequently entered judgment in favor of Respondents. DRR timely appealed.

DISCUSSION

I

STANDARD OF REVIEW

The standard of review for an order granting a motion for summary judgment is de novo. (*Aguilar v. Atlantic Richfield Co.* (2001) 25 Cal.4th 826, 860 (*Aguilar*).)

In performing our independent review, we apply the same three-step process as the trial court. "Because summary judgment is defined by the material allegations in the pleadings, we first look to the pleadings to identify the elements of the causes of action for which relief is sought." (*Baptist v. Robinson* (2006) 143 Cal.App.4th 151, 159 (*Baptist*).)

"We then examine the moving party's motion, including the evidence offered in support of the motion." (*Baptist, supra*, 143 Cal.App.4th at p. 159.) A defendant moving for summary judgment has the initial burden of showing that a cause of action lacks merit because one or more elements of the cause of action cannot be established or there is a complete defense to that cause of action. (Code Civ. Proc., § 437c, subd. (o); *Aguilar, supra*, 25 Cal.4th at p. 850.)

If the defendant fails to make this initial showing, it is unnecessary to examine the plaintiff's opposing evidence and the motion must be denied. However, if the moving papers make a prima facie showing that justifies a judgment in the defendant's favor, the burden shifts to the plaintiff to make a prima facie showing of the existence of a triable issue of material fact. (§ 437c, subd. (p)(2); *Aguilar, supra*, 25 Cal.4th at p. 849; *Kahn v. East Side Union High School Dist.* (2003) 31 Cal.4th 990, 1002-1003.)

In determining whether the parties have met their respective burdens, "the court must 'consider all of the evidence' and 'all' of the 'inferences' reasonably drawn therefrom [citations], and must view such evidence [citations] and such inferences [citations], in the light most favorable to the opposing party." (*Aguilar, supra*, 25 Cal.4th at p. 843.)

"There is a triable issue of material fact if, and only if, the evidence would allow a

reasonable trier of fact to find the underlying fact in favor of the party opposing the motion in accordance with the applicable standard of proof." (*Id.* at p. 850, fn. omitted.) Thus, a party "cannot avoid summary judgment by asserting facts based on mere speculation and conjecture, but instead must produce admissible evidence raising a triable issue of fact." (*LaChapelle v. Toyota Motor Credit Corp.* (2002) 102 Cal.App.4th 977, 981.)

II

AIDING AND ABETTING BREACH OF FIDUCIARY DUTY

A. Respondents' Motions for Summary Judgment

Hagenbuch filed his own motion for summary judgment. Wachtel, EuroAmerican, Knobel, and the Trust filed a combined motion for summary judgment. Respondents' respective motions focused on the lack of any disputed material fact that they had knowledge of the alleged breach of fiduciary duty. (See *Nasrawi v. Buck Consultants LLC* (2014) 231 Cal.App.4th 328, 343 (*Nasrawi*).)

B. The Elements of the Cause of Action and DRR's Allegations

"The elements of a claim for aiding and abetting a breach of fiduciary duty are: (1) a third party's breach of fiduciary duties owed to plaintiff; (2) defendant's actual knowledge of that breach of fiduciary duties; (3) substantial assistance or encouragement by defendant to the third party's breach; and (4) defendant's conduct was a substantial factor in causing harm to plaintiff." (*Nasrawi, supra*, 231 Cal.App.4th at p. 343.) Unlike liability for a civil conspiracy, a defendant may be liable for aiding and abetting the breach of a fiduciary duty even though the defendant did not itself owe that duty to the

plaintiff. (*American Master Lease LLC v. Idanta Partners, Ltd.* (2014) 225 Cal.App.4th 1451, 1476.) Thus, when a defendant does not owe a duty to the plaintiff, that defendant also must make " ' "a conscious decision to participate in tortious activity for the purpose of assisting another in performing a wrongful act." ' "8 (*Id.* at p. 1477, citing *Berg & Berg Enterprises, LLC v. Sherwood Partners, Inc.* (2005) 131 Cal.App.4th 802, 823, fn. 10.)

Here, for purposes of summary judgment, the parties do not quibble about the existence of a breach of fiduciary duty. Nevertheless, they disagree about what constituted the breach. This disagreement is critical to the issue before us.

"California courts have long held that liability for aiding and abetting depends on proof the defendant had actual knowledge of the specific primary wrong the defendant substantially assisted." (*Casey v. U.S. Bank Nat. Assn.* (2005) 127 Cal.App.4th 1138, 1145; see *Nasrawi, supra*, 231 Cal.App.4th at p. 343 [observing that in the context of considering a demurrer to an aiding and abetting breach of fiduciary duty claim, the court must first identify precisely the breach of fiduciary duty for which plaintiff seeks to hold the defendant liable].). "In the civil arena, an aider and abettor is called a cotortfeasor.

8 The superior court also found that Respondents established the absence of triable issues of material fact as to the "conscious decision" element of the aiding and abetting cause of action. It did not engage in extensive analysis on this issue, but concluded that the same facts and evidence that supported Respondents' argument regarding the knowledge element also supported summary judgment on the "conscious decision" element as well. The parties did not brief this issue in much detail, if at all, but there appears to be some disagreement on whether there is a "conscious decision" element in an aiding and abetting claim. Although there appears to be some consensus under California law that there is, we need not weigh in on that issue because we conclude summary judgment is appropriate on the knowledge element.

To be held liable as a cotortfeasor, a defendant must have knowledge . . . defendant can be held liable as a cotortfeasor on the basis of acting in concert only if he or she knew that a tort had been, or was to be, committed." (*Gerard v. Ross* (1988) 204 Cal.App.3d 968, 983.) Thus, the identification of the specific breach of duty is essential here. It must be precisely identified so we can determine whether a triable issue of material fact exists as to Respondents' knowledge of the breach.

The superior court found that the breach of fiduciary duty that Respondents allegedly aided and abetted was Katz's "scheme" "to steal the business away from its existing public shareholders by saddling [MicroIslet] with expensive debt that could not be repaid." In its opening brief, DRR explains this theory of breach by arguing the Lenain Memo and Term Sheet illuminate the illicit scheme. Respondents assert DRR is changing its theory on appeal. They contend DRR's alleged breach was that Katz and the other insiders caused MicroIslet to take on "toxic" loans while turning down available, more favorable equity financing. We turn to the operative complaint to resolve this dispute because "[t]he pleadings set the boundaries of the issues to be resolved at summary judgment." (*Oakland Raiders v. National Football League* (2005) 131 Cal.App.4th 621, 648.) Indeed, the allegations of the operative complaint define the scope of the issues on summary judgment. (*Couch v. San Juan Unified School Dist.* (1995) 33 Cal.App.4th 1491, 1499.)

In the operative complaint, while discussing the cause of action for aiding and abetting breach of fiduciary duty, DRR alleged that Katz had a "plan to steal the business away from its existing public shareholders by saddling [MicroIslet] with expensive debt

that could not be repaid." More specifically, DRR alleged that Respondents "had specific knowledge from Katz and his co-conspirators that MicroIslet was on the verge of becoming immensely valuable and that Katz and his new team of officers, directors, and creditors had a scheme developed to use their control to wrench ownership away from the public shareholders, all with an expected massive profit for themselves." DRR further averred that this scheme was outlined in the Lenain Memo. Put differently, the recapitalization plan was the culmination of Katz's scheme to steal MicroIslet's business.

DRR also alleged "that after Katz and his crew loaded their debt onto MicroIslet and had fully developed their takeover scheme, complete with legal advice documented in the Lenain [M]emo on how to formally accomplish their scheme, Katz and other new creditor defendants approached Hagenbuch to join their scheme in order to make the debt harmonization approach work smoothly and consistently and, because Hagenbuch owed the only other large outstanding debt owed by MicroIslet besides the new debt layered on by Katz and crew, to avoid likely confrontation and challenge, Hagenbuch received the Lenain [M]emo and debt harmonization agreement."

Therefore, in the operative complaint, DRR clearly referred to the Lenain Memo and the recapitalization plan in the FAC. That said, the FAC also mentioned the insiders causing MicroIslet to take on loans instead of pursuing available equity financing. For example, as part of its allegations of aiding and abetting breach of fiduciary duty, DRR incorporated other paragraphs of the FAC. One such paragraph also described the breach of fiduciary duty to include forgoing other forms of financing: "Rather than seeking or accepting available funding for [MicroIslet] at competitive market rates or on favorable

terms from existing shareholders and others, the Defendants [Katz and the other corporate insiders] arranged to make loans themselves or through friends and related parties and to provide financing to [MicroIslet] on terms unfavorable and unfair to the business, all designed to cause the debt to go unpaid so that the Defendants would take over most or all of the ownership of the business from existing shareholders." These allegations make clear that part of the alleged breach was declining to pursue certain avenues of funding in favor of "toxic" loans from Respondents.

In fact, these allegations are consistent with other representations DRR made to the superior court. For example, in opposing demurrers to the original complaint, DRR underscored the wrong it believed was committed: "The harm DRR is complaining of is Defendants eschewing available, more favorable financing in place of extremely high interest rate debt to insiders and their affiliates; the toxic nature of this insider debt made it impossible to raise further necessary financing from outside sources, which ultimately caused the company to fail (as intended by Defendants)."

In opposing a special motion to strike, DRR made a similar argument: "Here, the principal thrust or gravamen of DRR's claim is that the defendants attempted to take effective control of MicroIslet by saddling it with toxic insider debt even though much more favorable equity financing options were available--a scheme that, if ultimately unsuccessful, nonetheless harmed the company and its balance sheet and capital structure as soon as the debt was placed in lieu of equity. Indeed, a review of the complaint

indicates that virtually all of its allegations concern the layering on of debt and the eschewing of available equity."⁹

Further, in DRR's opening brief here, it emphasizes that equity financing was available to MicroIslet. For example, DRR represented that 2007 and 2008 were "very good years for financing biotech companies, including equity financing." DRR also maintains that two brokers at Dawson James Securities (Charles Robinson and Howard Roth), were MicroIslet shareholders who approached MicroIslet management about "easily" raising funds for the company, but management declined. Also, DRR asserts that the officers and directors "put-off" several interested equity investors in 2008. It is clear from its arguments in its opening brief, DRR considered the wrongful scheme to include the officers and directors shunning available equity financing while causing the company to take on loans with burdensome terms. Indeed, such financing decisions were critical to Katz's scheme.

⁹ Moreover, the superior court's order denying the special motion to strike was appealed to this court. In affirming the superior court's order, we observed, "It is clear from the allegations of the complaint that the principal thrust or gravamen of DRR's causes of action is that appellants engaged in a scheme to enable the creditor defendants to take over MicroIslet by 'saddling' it with unfavorable insider debt even though more favorable equity financing options were available to the company. . . . DRR alleged that the creditor defendants provided loans to MicroIslet with onerous terms that were approved by the director/officer defendants, the director/officer defendants eschewed more attractive and available equity financing, and the director/officer defendants engaged in acts designed to conceal their misdeeds." (See *Diabetes Research Restitution, LLC v. Katz* (Feb. 11, 2014, D062586) [nonpub. opn.].) Thus, in the previous matter before us, we determined that the "scheme" to recapitalize the company consisted of three parts. First, loans were provided to the company on onerous terms. Second, the directors and officers declined more attractive and available equity financing. Third, the officers and directors concealed their misdeeds.

Thus, in addition to the allegations in the FAC, DRR made at least two representations to the superior court that the breach of fiduciary duty consisted of the insiders pursuing unfavorable loans instead of available, friendlier financing.¹⁰ This is the same theory that was echoed in its opening brief here. We view these representations as consistent with the allegations in the FAC. Further, they help to define precisely what wrong DRR alleged the officers and directors committed.

In its reply brief, DRR claims that it did not allege that Respondents knew that the officers and directors were turning down other investors. And as such, DRR insists that it did not have to create a triable issue of fact as to Respondents' actual knowledge of that act. Indeed, DRR concedes that it has no evidence that Respondents had any such knowledge. DRR argues this concession is not of the moment because it has substantial evidence supporting a conclusion that Respondents knew of the officers and directors' acts to harm MicroIslet with toxic loans and a "wrongful takeover scheme."

However, DRR's argument begs the question: What precisely is the wrongful takeover scheme? Simply pointing to the recapitalization plan as set forth in the Lenain Memo and Term Sheet does not adequately answer this question. On its face, the Lenain Memo does not indicate that anything afoul was afoot. The Lenain Memo was written by MicroIslet's outside counsel and it purports to summarize the initial recommendation of

¹⁰ Based on these representations, Hagenbuch urges us to conclude that DRR is judicially estopped from arguing that the breach of fiduciary duty was Katz's scheme to take over MicroIslet through a recapitalization plan. (See *Scripps Clinic v. Superior Court* (2003) 108 Cal.App.4th 917, 943.) We decline to do so because the basis of DRR's claims against Respondents is set forth in the FAC, and the subject representations echo the operative complaint's allegations.

the special committee. Katz was not a member of the special committee. There is no indication in the record that Katz played any role in devising the specific plan outlined in the Lenain Memo. Put differently, the Lenain Memo, by itself, does not represent a breach of fiduciary duty.

We have similar concerns regarding the Term Sheet's limited impact on the issues before us. That document set forth terms for a proposed recapitalization¹¹ of MicroIslet. It explicitly states that it was "prepared for the purpose of seeking indications of interest only." The Term Sheet further clarified: "There is no obligation on the part of any party until definitive documents are signed by all parties, which definitive agreements shall be subject to the review and approval of the MicroIslet, Inc. Board of Directors. This Term Sheet does not constitute an offer to sell or a solicitation of an offer to purchase securities." There is nothing in the Term Sheet that indicates that Katz had engaged in or was engaging in a "wrongful takeover scheme." To understand that Katz was engaged in such a ploy, one would need to know how the company arrived at the decision to recapitalize. In other words, what acts created the circumstances that lead the board to consider a recapitalization plan?

¹¹ No party takes the position that the directors and officers pursuing a recapitalization plan would per se be a breach of fiduciary duty. Indeed, a company may benefit from such a plan (especially if the plan would eliminate debt and encourage new investment). However, a recapitalization plan could dilute the ownership interest of other shareholders, and under such a scenario, those shareholders might have a claim against the directors and officers. But that claim would not belong to the company. (See *Jara v. Suprema Meats, Inc.* (2004) 121 Cal.App.4th 1238, 1254-1258.) Thus, because DRR only purchased MicroIslet's prebankruptcy claims, it does not have standing to allege any claims belonging to shareholders.

DRR believes that the directors and officers engaged in a wrongful takeover scheme by saddling the company with debt it could not repay. They argue we should focus on this theory only. But underlying its theory is the implication that the officers and directors did not need to borrow money from Respondents to keep MicroIslet in business. Yet, it is undisputed that MicroIslet had no revenue stream and needed money to operate. In fact, it ultimately filed for bankruptcy because it ran out of money. Clearly, MicroIslet needed to obtain funding at the time in question. Thus, DRR claims other sources of funding, especially equity investments, were available to MicroIslet at that time, but the officers and directors ignored such opportunities and borrowed money instead. This is the crux of the wrongful takeover scheme. Although other funding was available, the officers and directors caused the company to take on toxic loans.

Borrowing money, even on less than favorable terms, by itself would not necessarily constitute a breach of fiduciary duty if other funding sources were not available to MicroIslet. DRR's theory of a breach of fiduciary duty requires the directors and officers to cause MicroIslet to take on loans with onerous terms while eschewing other available funding. As that is the specific primary wrong at issue here, we must determine if a triable issue of material fact exists as to Respondents' actual knowledge of that precise breach. (See *Casey v. U.S. Bank Nat. Assn.*, *supra*, 127 Cal.App.4th at p. 1145; *Nasrawi*, *supra*, 231 Cal.App.4th at p. 343.) To avoid summary judgment, there must be sufficient evidence to allow a reasonable inference that Respondents knew the unfavorable loans and resulting recapitalization plan were *wrongful* because the company had better options.

C. Respondents

1. *Hagenbuch*

Hagenbuch offered evidence that he did not have any knowledge of Katz's alleged scheme to steal MicroIslet's business. To this end, he submitted his declaration stating that he lacked the necessary knowledge to have aided and abetted any breach of fiduciary duty. Specifically, Hagenbuch stepped down as chairman of MicroIslet in June 2007, before Katz became involved in the running of MicroIslet and the alleged scheme began. He did not make any loans to MicroIslet after he left the company. Hagenbuch did not solicit any of the subject "toxic" loans. He did not negotiate or approve the terms of any of the "toxic" loans. MicroIslet's officers and/or directors did not inform Hagenbuch or seek his approval before they arranged and approved any of the loans at issue. Moreover, the same officers and/or directors did not inform Hagenbuch before they turned down any available offer of equity financing. DRR did not dispute any of these facts.

Through his declaration, Hagenbuch also offered evidence that MicroIslet officers and directors did not tell him that they had decided to turn down equity financing in favor of loans. In addition, he declared that no one had informed him that anyone had made an offer of equity financing for MicroIslet after June 2007. Also, Hagenbuch stated that he had no knowledge of any alleged scheme to steal MicroIslet's business.

Based on this evidence, we conclude that Hagenbuch satisfied his initial burden of showing that DRR cannot prove at least one element (actual knowledge of the breach of fiduciary duty) of its aiding and abetting claim. (*Aguilar, supra*, 25 Cal.4th at p. 850.)

We thus move on to the next step to determine whether DRR made a prima facie showing of the existence of a triable issue of material fact. (*Id.* at p. 849.)

We begin our discussion of DRR's evidence in an unorthodox manner by briefly discussing what it is not. DRR offers no evidence that Hagenbuch played any role in MicroIslet's officers and directors' decision to accept the "toxic" loans. Nor does DRR provide any evidence that Hagenbuch was privy to any scheme to saddle the company with too much debt. Further, DRR points to nothing in the record that indicates that Hagenbuch was aware that the officers and directors were declining available equity financing. Instead, DRR focuses this court on three pieces of evidence it claims create a triable issue of fact as to Hagenbuch's knowledge of the alleged breach of fiduciary duty. As we discuss below, we find DRR's arguments wanting.

First, DRR maintains that Hagenbuch, in late 2006, when he was the chairman of MicroIslet, developed the "scheme" to recapitalize the company that was eventually adopted by Katz. To this end, DRR offered a November 20, 2006 memorandum from Hagenbuch to the company's board of directors, Steel, and John Tishler.¹² In that memorandum, Hagenbuch discussed MicroIslet's historical financing efforts and explained the difficulty of raising additional funds going forward because of the company's increasing cash needs as well as its lack of revenue stream or marketable product. Indeed, Hagenbuch cautioned that MicroIslet would be out of money sometime in March 2007. Hagenbuch discussed various funding strategies, but ultimately

¹² John Tishler, an attorney with Sheppard Mullin, represented MicroIslet in November 2006.

recommended the board "start to plan a recapitalization of [MicroIslet] which will result in substantial dilution to our existing shareholders, but would leave us in the game, with no debt and hopefully with sufficient cash." Hagenbuch asked for others' thoughts on his viewpoint and asked that additional ideas be shared with the board of directors.

We see two primary problems with DRR's claim that Hagenbuch's November 20, 2006 memorandum was the genesis of Katz's scheme to steal the business. According to DRR, the key component of Katz's scheme was causing MicroIslet to take on the "toxic" loans. In contrast, in his memorandum, Hagenbuch warned of the dangers of debt financing and the possibility of "giving up control of the company to the note holders." He did not advocate for debt financing. In fact, Hagenbuch stressed that a possible recapitalization plan could leave the company debt free. As such, Hagenbuch's recapitalization plan did not contain the most important element of Katz's scheme. There was no indication that Hagenbuch wanted the company to take on loans with onerous terms.

In addition, Hagenbuch's memorandum was written well before Katz replaced Hagenbuch as MicroIslet's chairman. And there is no evidence in the record that Hagenbuch ever shared the November 26, 2006 memorandum with Katz. DRR attempts to address this shortcoming by claiming that on July 30, 2008, Hagenbuch sent a proposal to MicroIslet like that contained in his November 2006 memorandum. This "proposal" was set forth in an e-mail to MicroIslet board member Mike Andrews suggesting a way to deal with MicroIslet's "most serious challenge" of "its inability to raise outside cash, coupled with a concern that [the] current funding sources will be unwilling or unable to

continue funding the Company." Hagenbuch's alternative was to "[d]o a pre-packaged bankruptcy filing" that would reduce the current equity stake in the company, convert debt to equity at a low valuation, and allow MicroIslet to offer new shares to investors at a lower pre-money valuation. Again, Hagenbuch's e-mail proposal lacks any discussion or suggestion that MicroIslet borrow additional funds at unfavorable rates. Alternatively stated, the vital feature of Katz's scheme (saddling the company with debt it could not repay) is not part of Hagenbuch's suggestion. Further, there is no indication in Hagenbuch's e-mail that he was aware of Katz's scheme to steal the business.

Second, DRR points to Hagenbuch's willingness to participate in the proposed recapitalization plan that was presented in the Term Sheet as support for its claim that Hagenbuch had knowledge of Katz's scheme. We disagree. As the superior court observed, this proposed recapitalization plan arose from a special committee appointed by MicroIslet's board of directors to study the idea of restructuring the company's ownership. MicroIslet's attorneys reviewed the recapitalization proposal. Even if we were to agree with DRR that the evidence shows that Hagenbuch was enthusiastic about participating in the proposed plan, such evidence does not show Hagenbuch had any knowledge of Katz's scheme to steal the business.

Third, DRR claims that Hagenbuch's renegotiation of his loans with MicroIslet shows that he had knowledge of Katz's scheme. Specifically, DRR offered evidence that on August 25, 2008, Hagenbuch signed two loan modification agreements that:

(1) changed the maturity date of the subject notes from January 12, 2008 to March 31, 2008; and (2) increased the interest rate from prime to 24 percent, retroactive to the date

of maturity. In deposition, Hagenbuch testified that he had an oral agreement with a MicroIslet director that he would not demand payment for a period of time. In addition, it was undisputed that (a) MicroIslet was in default on Hagenbuch's loans for about eight months before the amendments; (b) the amendments extended the maturity dates of the loans, decreasing the length of time the loans were in default; (c) after the amendments, Hagenbuch did not force MicroIslet to repay the loans; and (d) MicroIslet never repaid any interest or principal on Hagenbuch's loans.

DRR characterizes the negotiation of the loan modifications as "anything but arm's length" and argues, without authority, that the modifications, in and of themselves, were unlawful. Additionally, DRR contends Hagenbuch's difficulty in explaining how he could negotiate such favorable terms for him to the detriment of MicroIslet somehow calls into question his credibility. In other words, Hagenbuch's failure to adequately explain how the loans were negotiated raises the possibility that a jury would not believe his testimony and could "conclude this circumstantially proved Hagenbuch ha[d] actual knowledge of insiders breaching their fiduciary duties and intended to assist it for his own gain." We agree with Hagenbuch that DRR's argument is mere speculation. In so agreeing, we determine that DRR's reliance on *Donchin v. Guerrero* (1995) 34 Cal.App.4th 1832 (*Donchin*) and *Heckman v. Ahmanson* (1985) 168 Cal.App.3d 119 (*Heckman*) is misplaced.

In *Donchin, supra*, 34 Cal.App.4th 1832, a case involving a dog bite, the plaintiff introduced undisputed evidence that the defendant had falsely told a third party that he did not know the dogs lived on his property. (*Id.* at p. 1841.) Noting that a false

exculpatory statement can serve as evidence of a defendant's "consciousness of liability," thereby "cast[ing] doubt on his denial of knowledge affecting his liability," the appellate court concluded that the defendant's initial false denial gave rise to a reasonable inference that the defendant had likewise lied about his prior knowledge of the dogs' vicious propensities. (*Id.* at pp. 1841, 1843.) Additionally, the plaintiff produced affirmative evidence that the defendant had actual knowledge of the dogs' vicious propensities. (*Id.* at pp. 1843-1845.)

No analogous facts exist here. DRR has not offered any evidence that Hagenbuch lied. Instead, DRR merely opines that his explanation of how he received the modified loan terms was "difficult to understand." Also, contrary to the plaintiff in *Donchin*, DRR has not presented affirmative evidence that Hagenbuch had knowledge of Katz's scheme to steal the business. In short, *Donchin, supra*, 34 Cal.App.4th 1832 is not instructive here.

Likewise, *Heckman, supra*, 168 Cal.App.3d 119 is not helpful to DRR. In that case, plaintiffs filed a motion for preliminary injunction asserting that a shareholder group who controlled 12 percent of the corporation was liable for breach of fiduciary duty under several theories, including aiding and abetting the corporate directors in breaching their fiduciary duties. (*Id.* at pp. 127-128.) At issue was an alleged greenmailing scheme whereby the shareholder group aided and abetted certain directors to allegedly breach their fiduciary duties by repurchasing the company's stock at inflated prices for retaining control of the company. (*Ibid.*) In determining a preliminary injunction was warranted, the court found the evidence showed the shareholder group:

(1) knew it was reselling its stock at a price considerably above market value to enable the Disney directors to retain control; (2) "knew or should have known" that the company would borrow \$325 million to purchase the stock; and (3) knew "[f]rom its previous dealings with Disney" that the increased debt load would damage Disney's stock price and credit score. (*Id.* at p. 127.)

Here, DRR has offered no analogous facts that Hagenbuch had actual knowledge of Katz's scheme, unlike the shareholder group in *Heckman, supra*, 168 Cal.App.3d 119. MicroIslet was in default on the Hagenbuch loans. Hagenbuch could have insisted on immediate repayment, something the company could not effect. His willingness not to do so, even in exchange for "onerous" extension terms, does not amount to aiding and abetting a breach of fiduciary duty absent some minimal evidence that he knew the company had another available financing alternative.

Also, in contrast to the *Heckman* shareholder group, Hagenbuch did not reap any benefits after he negotiated the loan modification as MicroIslet never repaid his loans. Additionally, Hagenbuch never converted the debt owed to him into equity. In summary, the facts in *Heckman, supra*, 168 Cal.App.3d 119, evidence a successful greenmailing scheme where the plaintiff provided evidence of the shareholder group's participation and knowledge of the scheme. Here, there is no such evidence. Instead, DRR asks this court to infer that Hagenbuch must have known of Katz's scheme or that he lacks credibility simply based on his renegotiation of the terms of his loans and his explanation of MicroIslet's reason for doing so.

We also note that, for the first time on appeal, DRR claims that the mere fact that Hagenbuch renegotiated his loans with MicroIslet causing the company to incur significant additional financial obligations to a third party in exchange for no benefit to the company was a breach of fiduciary duty as well. Alternatively stated, DRR now asserts an additional breach of fiduciary duty by the directors and officers agreeing to new loan terms for Hagenbuch. And by Hagenbuch signing the loan modification agreements, he was aiding and abetting this new breach. We need not address theories that were not raised in the pleadings (*Williams v. California Physicians' Service* (1999) 72 Cal.App.4th 722, 738), and a plaintiff may not defeat a summary judgment motion by producing evidence to support claims outside the issues framed by the pleadings. (*City of Hope Nat. Medical Center v. Superior Court* (1992) 8 Cal.App.4th 633, 639.) As such, we decline to consider these newly raised theories of liability.¹³

2. Wachtel

Wachtel submitted evidence, through his declaration, of the following. He is the president and sole shareholder of EuroAmerican. He learned of MicroIslet from Katz, who was Wachtel's friend and a client of Wachtel's law firm. Katz told Wachtel that MicroIslet was attempting to raise equity capital from investors, but needed short term

¹³ To create a triable issue of fact, DRR offered other evidence regarding how poorly Hagenbuch ran MicroIslet while he was the director, including his approach to obtaining financing for the company. DRR does not explain how this evidence relates to Hagenbuch's knowledge of Katz's scheme to steal the business. Similarly, we do not consider tangential evidence offered by Hagenbuch regarding DRR's motives in suing him. For example, Hagenbuch claims that DRR asked him to fund the instant litigation and sought him as an additional plaintiff. When he refused, DRR added him as a defendant.

financing to continue its operations until it could raise equity capital. Katz asked Wachtel to lend money to MicroIslet.

Wachtel did not conduct extensive due diligence before investing in MicroIslet, but instead, relied on Katz as a friend and business associate. Wachtel did review one of MicroIslet's quarterly or annual reports and noticed that it appeared the company owed a lot of money to different creditors on different terms. He then told Katz that, in his experience, it would be difficult for MicroIslet to raise equity capital unless the terms of the company's debts were harmonized. Wachtel thus urged Katz to hire corporate counsel for MicroIslet to assist in that process.

MicroIslet retained Foley & Lardner, and Katz forwarded Wachtel a copy of the Lenain Memo and later the Term Sheet proposing a loan harmonizing transaction. At Katz's request, Wachtel caused EuroAmerican to loan over \$900,000 to MicroIslet. These loans bore a 10 percent interest rate, which increased to 24 percent in the event of default.¹⁴ In addition, EuroAmerican loaned an additional \$422,000 directly to Katz, which he in turn reloaned to MicroIslet. These loans bore an interest rate of about eight percent because Katz was personally liable to repay them.

When Wachtel caused EuroAmerican to loan money to MicroIslet and Katz, he did so in reliance on Katz's statement that MicroIslet was seeking equity investors and

¹⁴ There was confusion in the record regarding the actual initial rate of EuroAmerican's loans to MicroIslet. Wachtel believed it was 10 or 12 percent while DRR argued it was 24 percent. None of the parties cite to a copy of the actual note or notes in the record. The disagreement regarding the initial rate of the subject loans does not create a triable issue of material fact as to the issues raised in this appeal.

needed only short term loans to keep operating until the equity capital could be raised. Wachtel had no knowledge or belief that Katz or anyone else on behalf of MicroIslet was declining offers of equity investment in MicroIslet.

In 2009, Wachtel learned that MicroIslet had filed a petition in bankruptcy court. Through EuroAmerican, he loaned an additional \$243,000 to MicroIslet to enable it to continue doing business during the bankruptcy proceeding. Because of MicroIslet's liquidation in bankruptcy, all EuroAmerican's prebankruptcy loans to MicroIslet were discharged. MicroIslet never paid EuroAmerican any interest or principal on the prebankruptcy loans. EuroAmerican also lost much of the money it loaned to MicroIslet after the bankruptcy filing. However, Katz paid off his loans with EuroAmerican.

Based on this evidence, we conclude that Wachtel satisfied his initial burden of showing that DRR cannot prove at least one element (actual knowledge of the specific breach of fiduciary duty) of its aiding and abetting claim. (*Aguilar, supra*, 25 Cal.4th at p. 850.) We thus move on to the next step to determine whether DRR made a prima facie showing of the existence of a triable issue of material fact. (*Id.* at p. 849.)

As a threshold matter, we note that DRR has pointed to no evidence that Wachtel was aware of any scheme from Katz to steal MicroIslet's business. Specifically, there is no evidence whatsoever that Wachtel knew that MicroIslet's officers and directors were turning down available financing while they were saddling the company with debt it could not repay. Instead, DRR insists that the terms of EuroAmerican's loans to Katz and later MicroIslet and Wachtel's explanation of these loans undermine Wachtel's credibility to such an extent that summary judgment was not proper. We disagree.

DRR breaks down the loans made by EuroAmerican into two categories. The first category consists of loans made from EuroAmerican to Katz directly. These loans were made beginning on April 18, 2008. EuroAmerican loaned the money to Katz at around eight percent simple interest. Katz then reloaned the funds to MicroIslet at 10 percent compound interest plus 24 percent penalty interest upon default.

Although DRR concedes that it has no evidence that Wachtel knew that Katz was loaning money he borrowed from EuroAmerican to MicroIslet at higher interest rates, it claims that Wachtel's explanation of why he loaned Katz the money was "difficult to understand," which creates an inference of actual knowledge of wrongdoing to support a claim for aiding and abetting a breach of fiduciary duty. To this end, DRR emphasizes that Wachtel claimed he caused EuroAmerican to loan money to Katz because he believed that Katz was more creditworthy than MicroIslet. However, DRR insists that Wachtel did not know any details about Katz's personal finances. In making this argument, DRR is not faithfully representing the record. During his deposition, Wachtel stated that he caused EuroAmerican to loan money to Katz instead of MicroIslet because it was a better credit risk to loan to Katz. Wachtel explained why this was so:

"Because I understood the financial condition of Ron Katz. He was a successful practicing accountant. He had a vibrant accounting firm. I don't know if at that time he'd already merged his firm into another accounting firm. [¶] By contrast, I did not have knowledge as to the financial condition of MicroIslet other than through what Ron Katz told me, hence my distinction."

Later during the deposition, Wachtel stated that he was not aware if Katz had ever filed bankruptcy. Moreover, it was implied that Katz had filed bankruptcy and Wachtel

appeared to be surprised by this news by responding, "Wow." Nevertheless, Wachtel's surprise that Katz had filed bankruptcy is far from knowing "no details about Katz'[s] personal finances" as DRR represents to this court. In short, Wachtel's lack of knowledge that Katz might have filed for bankruptcy does not call into question Wachtel's credibility. Such a lack of knowledge falls short of anything approaching the false exculpatory statement in *Donchin, supra*, 34 Cal.App.4th at page 1841.

In addition, we are not persuaded by DRR's claim that Wachtel admitted that the "common approach" was to loan money directly to a company with a personal guarantee from a board member and this admission somehow calls into question Wachtel's testimony that he did not know that Katz was reloaning the money he borrowed at a higher interest rate to MicroIslet. The fact that Wachtel used a less common approach to loan money to Katz directly does not impute to Wachtel knowledge that Katz would loan the money to MicroIslet at a higher interest rate. Nor does it call into question Wachtel's credibility.

In summary, this evidence offered by DRR does not create a triable issue of material fact as to Wachtel's actual knowledge that Katz was engaged in a scheme to steal MicroIslet's business.¹⁵

¹⁵ In addition, for the first time on appeal, DRR appears to be arguing that EuroAmerican's loans to Katz allowed him to commit waste, and thus, breach his fiduciary duty in this manner. As such, per DRR, Wachtel and EuroAmerican were aiding and abetting this breach simply by loaning money to Katz. This is a new theory not raised in the pleadings, and we decline to address it. (See *Williams v. California Physicians' Service, supra*, 72 Cal.App.4th at p. 738; *City of Hope Nat. Medical Center v. Superior Court, supra*, 8 Cal.App.4th at p. 639.) Further, there is no evidence that

The second category of loans consists of the loans EuroAmerican made directly to MicroIslet. After Wachtel received the Lenain Memo and the Term Sheet, he decided to cause EuroAmerican to loan more than \$900,000 directly to MicroIslet. DRR claims that these two documents somehow informed Wachtel about Katz's wrongful takeover scheme. However, DRR does not point to any language in the documents to support this assertion. Nevertheless, DRR contends that Wachtel offered no justification for his decision to start loaning money directly to MicroIslet; thus, he must have done so because he learned that the company was considering converting its debt into equity as set forth in the Lenain Memo and Term Sheet. We are not persuaded.

The Lenain Memo was the product of a special committee meeting to explore "recapitalization alternatives in light of the Company's current capital structure and funding needs" Outside counsel drafted the memorandum as a summary of the committee's initial recommendation. There is no indication in the record that Katz played any role in formulating the committee's recommendation. Further, there is nothing nefarious about the memorandum itself and the fact that Wachtel saw it does not create a triable issue of fact regarding his knowledge of the alleged breach of fiduciary duty. Contrary to the suggestion that the Lenain Memo revealed Katz was in the process of his wrongful takeover scheme, it rather lends credence to Wachtel's claim that Katz told him the company needed short term financing until it could secure additional equity funding.

Wachtel was aware that Katz was going to reloan the money to MicroIslet at a higher interest rate. Alternatively stated, even if we were to accept this new theory of a breach of fiduciary duty, DRR has not established a triable issue of fact regarding whether Wachtel knew Katz was going to commit waste.

The plan summarized in the Lenain Memo explained an avenue by which the company could raise additional equity funds.

Likewise, the fact that Katz sent Wachtel the Term Sheet does not create a triable issue of fact regarding Wachtel's actual knowledge that directors and officers had breached their fiduciary duties. We agree with the superior court that the Term Sheet "came as a result of a meeting of a Special Committee of the Board and [was] reviewed by MicroIslet attorneys. This proposal alone, or in conjunction with the other evidence [DRR] presents, does not support a finding of [Respondents'] knowledge of the . . . alleged 'scheme to steal the business.' " The Term Sheet merely indicated that the board was considering a recapitalization plan, and the board was doing so before Wachtel caused EuroAmerican to loan money to MicroIslet. Thus, DRR cannot argue that EuroAmerican's loans to MicroIslet helped create the necessary conditions for the board to approve a recapitalization plan, which would allow Katz to steal the company's business. The plan was already recommended before Wachtel had EuroAmerican loan any money to the company. Alternatively stated, the Term Sheet is not proof that Wachtel had knowledge of Katz's wrongful takeover scheme and knowingly aided and abetted it by loaning MicroIslet money. Neither the Lenain Memo nor the Term Sheet is the talisman to create a triable issue of fact as to Wachtel's knowledge.¹⁶

¹⁶ DRR's scattershot approach to trying to create a triable issue of fact is underscored by its final argument as to Wachtel. DRR places great importance on the fact that Wachtel agreed in advance to serve as a debtor-in-possession lender in MicroIslet's bankruptcy. DRR claims the funds lent by EuroAmerican to MicroIslet in bankruptcy could have allowed MicroIslet to avoid bankruptcy if invested as equity before filing.

DRR additionally emphasizes that the loans EuroAmerican made to MicroIslet had "suspiciously high interest rates and short maturities" as well as "terms [that] were not negotiated so much as simply given away by Katz." And DRR insists each time Katz asked for money, "no matter the amount or circumstances," Wachtel did as Katz requested, with no questions asked and no terms negotiated. Indeed, according to DRR, Wachtel did so despite being a sophisticated investor, which calls into question his credibility. However, DRR is not offering evidence of Wachtel's knowledge. It is merely speculating based on "suspicious" circumstances. "[S]uspicion and surmise do not constitute actual knowledge." (*Casey v. U.S. Bank Nat. Assn.*, *supra*, 127 Cal.App.4th at p. 1147.)

Nevertheless, DRR maintains this evidence raises a triable issue of fact as to Wachtel's actual knowledge because Wachtel "had to know Katz was not serving the interests of MicroIslet because Katz should have at least attempted to obtain equity financing or to negotiate better loan terms, and any minimally experienced investor or attorney would know this." However, Wachtel offered evidence that Katz told him that MicroIslet needed short term loans while it looked for equity financing. Thus, per Wachtel, he believed Katz was trying to obtain equity financing on behalf of MicroIslet, not declining to do so as DRR claims.

DRR does not adequately explain the significance of this argument, and we struggle to comprehend how this assertion creates a triable issue of material fact as to Wachtel's knowledge of the subject breach of fiduciary duty. There is nothing in the record indicating Wachtel was interested in making an equity investment or was asked to make an equity investment in MicroIslet. In addition, there is no evidence in the record that the amount of EuroAmerican's loan to MicroIslet would have allowed MicroIslet to avoid bankruptcy.

In addition, DRR insists that a jury could find Wachtel not credible because friends, like Katz and Wachtel, "would absolutely share details and discuss the circumstances of what Katz was doing, and consequently reflecting guilty knowledge of by Wachtel's denial of any knowledge." DRR continues with this theory by arguing that Wachtel made the loans knowing that MicroIslet would not repay them and the existence of the debt of MicroIslet's books would effectively prevent the company from obtaining equity financing. Therefore, Wachtel causing EuroAmerican to loan money to MicroIslet helped create the conditions necessary for Katz to realize his scheme to steal the business. Yet, as we discuss above, those conditions already existed and induced the board to consider a recapitalization plan before Wachtel caused EuroAmerican to loan money to the company.

Finally, DRR, relying on *In re Del Monte Foods Co. Shareholders Litigation* (Del. Ch. 2011) 25 A.3d 813 (*Del Monte*), contends that the absence of legitimate bargaining at arm's length is evidence of an improper state of mind. It contends that a third party is free to seek the best possible deal through arms' length negotiations but " 'it may not knowingly participate in the . . . board's breach of fiduciary duty by extracting terms which require the opposite party to prefer its interests at the expense of shareholders.' " (*Id.* at p. 837.) Therefore, DRR claims that we can infer Wachtel's knowledge of Katz's scheme simply because the loan terms were so onerous. DRR's reliance on *Del Monte* is misplaced.

In *Del Monte*, 25 A.3d 813, a third party bidder knowingly violated a confidentiality agreement and secretly manipulated the sales processes of a merger deal

involving a leveraged buyout of stockholders in Del Monte Food Company. (*Id.* at pp. 816-817, 837). It further knowingly participated in the creation of a conflict of interest for the company's financial advisor. (*Ibid.*) The Court of Chancery found these acts sufficient to establish the likelihood of plaintiffs' success on the merits in their claim that the bidder aided and abetted the subject breaches of fiduciary duty. No such analogous facts exist here. Wachtel did not create a conflict of interest for Katz or any of the other members of the board by demanding certain loan terms. To the contrary, there is no indication that Wachtel demanded any specific terms or even sought out the lending opportunity. Instead, Katz asked Wachtel to loan money to MicroIslet and offered terms. Wachtel accepted. Wachtel did not breach a confidentiality agreement or secretly manipulate MicroIslet's financing process. Further, the chancery court specifically found that the bidder had knowledge of the other defendant's self-interested activities. (*Id.* at p. 837.) No such knowledge on behalf of Wachtel has been shown to exist here. In short, *Del Monte* does not stand for the proposition that a triable issue of material fact as to Wachtel's knowledge of the breach of fiduciary duty exists simply because Wachtel agreed to have EuroAmerican loan money to MicroIslet per the terms offered by Katz.¹⁷

In summary, we determine that DRR has not carried its burden of producing admissible evidence creating a triable issue of fact as to Wachtel and EuroAmerican. Summary judgment therefore was appropriate.

¹⁷ For similar reasons, *Del Monte, supra*, 25 A.3d 813 does not create liability for Hagenbuch based on his loan term renegotiation or Knobel for agreeing to loan money to MicroIslet when asked by Katz.

3. Nobel

Knobel submitted evidence, through his declaration, of the following. Nobel was one of the trustees of the Trust. In 2003, Katz, who was a business and personal acquaintance of Nobel, introduced Nobel to MicroIslet. That year, Nobel began to buy shares of stock of MicroIslet, both personally and on behalf of the Trust. Between 2003 and 2008, he purchased hundreds of thousands of shares.

In 2007, Katz asked Nobel to loan money to MicroIslet. Katz told Nobel that MicroIslet needed additional funds to continue its efforts to develop a successful product. In response to Katz's request, Nobel loaned \$1 million to MicroIslet in September 2007. Nobel stated that, at that time, he had no knowledge or belief that Katz or anyone else on behalf of MicroIslet was turning down offers of equity investment in MicroIslet. In June 2008, again in response to a request from Katz, Nobel caused the Trust to loan \$500,000 to MicroIslet. Nobel again stated that, at that time, he had no knowledge or belief that Katz or anyone else on behalf of MicroIslet was turning down any offer of equity investment in MicroIslet.

In September 2008, Nobel received the Term Sheet. Nobel never signed any documents accepting the proposed recapitalization and the proposed recapitalization never took place. Neither Nobel nor the Trust ever converted any of their loans to MicroIslet stock. MicroIslet did not repay the loans made by Nobel or the Trust, and thus, Nobel lost the \$1 million he loaned, and the Trust lost the \$500,000 it loaned. Nobel also declared that when he loaned money to MicroIslet or caused the Trust to do

so, he did so in good faith and in reliance on Katz's representations that the funds were necessary to keep MicroIslet running until additional equity could be raised.

Based on this evidence, we conclude that Knobel satisfied his initial burden of showing that DRR cannot prove at least one element (actual knowledge of the breach of fiduciary duty) of its aiding and abetting claim. (*Aguilar, supra*, 25 Cal.4th at p. 850.) We thus move on to the next step to determine whether DRR made a prima facie showing of the existence of a triable issue of material fact. (*Id.* at p. 849.)

DRR claims that Knobel aided and abetted the breach of fiduciary duty by loaning money to MicroIslet at Katz's request and aiding Katz in his takeover scheme. To this end, DRR argues that, given Knobel's background, education, and experience, Knobel would know his loans were highly unusual in their terms. DRR then contends "no sane person" would make such a second large loan from the Trust to the same company that was in default on Knobel's previous loan. DRR concludes that Knobel's loans "were wrongful, a breach by Katz of his fiduciary duties, and acts by Knobel in aiding the breach." In this sense, DRR appears to argue that Knobel's decision to loan money to MicroIslet reflected such poor judgment from a sophisticated investor that he must have known that his loans were bad for MicroIslet.¹⁸ Accordingly, DRR states several times in its opening brief that Knobel explained his conduct by stating that he was acting "stupid" and "ridiculous," and as such, his testimony that he did not know of Katz's

¹⁸ Even if Knobel believed his loans to MicroIslet were not favorable to the company, such knowledge does not establish that he was aware of Katz's wrongful takeover scheme.

scheme is not credible. However, Knobel's comments do not call into question his credibility.

During his deposition, Knobel was asked how it came to be that MicroIslet owed him and the Trust more money than anyone else except for Hagenbuch. Knobel responded, "Ronnie Katz would call from time to time and I -- today sitting in this chair, stupidly said yes." Knobel was commenting on his decision to loan money to MicroIslet with the benefit of hindsight. Having loaned a substantial amount of money for which he was not repaid and then getting sued based upon those defaulted loans, it logically follows that Knobel would believe his decision to loan money to MicroIslet was foolish. We disagree that this characterization of his past action considering his present circumstances somehow raises doubt as to Knobel's credibility.

Later during his deposition, Knobel was asked if he researched MicroIslet before making an initial equity investment. Knobel said that he did not, stating that his approach "may seem ridiculous" but he invested because Katz, a "prominent accountant," asked him to do so and he learned that Stephen Ross, who is worth \$6 billion and "has proven to be a very shrewd investor" had already invested in the company. Knobel thus used the term "ridiculous" in reference to his decision to initially invest in MicroIslet, not loan money to it. In any event, Knobel's comment that his investment decision may seem ridiculous does not create a triable issue of material fact as to his actual knowledge of Katz's scheme to wrongfully take over the company.

In addition, DRR offers no authority or cogent argument that Knobel's mere loaning of money to MicroIslet, even if the terms were unfavorable to the company,

supports the claim that Knobel knew of Katz's specific breach of fiduciary duty. There is no evidence that Knobel was aware that MicroIslet was accepting his loans to the exclusion of available equity financing.

DRR also contends that Knobel's receipt of the Term Sheet and his execution of same showed that he was helping Katz with his takeover scheme. DRR's argument overlooks the fact that Knobel and the Trust made their loans before ever receiving the Term Sheet. Thus, the Term Sheet cannot show what Knobel knew when he loaned the money to MicroIslet. In short, DRR has no evidence that creates a triable issue of material fact as to whether Knobel had actual knowledge of the specific breach of fiduciary duty. DRR's contention that Knobel knew of Katz's scheme is little more than an assumption that Knobel should have known or had to know because of his experience, sophistication, and friendship with Katz. This is speculation not evidence. Summary judgment was appropriate as to Knobel and the Trust.

4. DRR's Expert Witness

DRR's final argument that the superior court erred in granting summary judgment rests entirely on the declaration of its expert witness, Douglas Johnston, Jr. He ultimately opines: "Those few investors and lenders to [MicroIslet] who did in fact fund the company over the period of 2007-2008 had to have known they were engaging in clandestine wrongdoing, collusive or otherwise, along with the officers and directors of the company." However, even if Johnston had the basis to form such an opinion, his opinion does not create a triable issue of fact as to whether Respondents had actual knowledge of the specific breach of fiduciary duty at issue here. In other words,

Johnston's declaration does not and cannot establish Respondents' actual knowledge of Katz's scheme to steal the business. He merely speculates that they must have known of some wrongdoing on behalf of the board and that their loans would make it more difficult for the company to obtain equity financing. DRR cannot fabricate a triable issue of fact through an expert witness's speculation. (See *McGonnell v. Kaiser Gypsum Co.* (2002) 98 Cal.App.4th 1098, 1106 ["Plaintiffs cannot manufacture a triable issue of fact through the use of an expert opinion with self-serving conclusions devoid of any basis, explanation or reasoning."]; accord *Andrews v. Foster Wheeler LLC* (2006) 138 Cal.App.4th 96, 108; *Nardizzi v. Harbor Chrysler Plymouth Sales, Inc.* (2006) 136 Cal.App.4th 1409, 1415.) Therefore, Johnston's declaration does not create a triable issue of material fact sufficient to overcome Respondents' motions for summary judgment.

DISPOSITION

The judgment is affirmed. Respondents are awarded their costs on appeal.

HUFFMAN, Acting P. J.

WE CONCUR:

NARES, J.

DATO, J.